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No. 84-1944

In the Supreme Court of the United States

OCTOBER TERM, 1985

UNITED STATES OF AMERICA, ET AL., APPELLANTS

v.

ALVIN HEMME, ET AL.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF ILLINOIS

BRIEF FOR THE UNITED STATES

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QUESTION PRESENTED

Whether, in computing the federal estate tax payable by the estate of a decedent who died on November 9, 1978, amendments to the federal tax laws passed by both houses of Congress on September 16, 1976, and approved by the President on October 4, 1976, may constitutionally be applied to ascertain the effect of gifts made by the decedent on September 28, 1976, and of an election made by him in a federal gift tax return filed on September 30, 1976.

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OPINION BELOW

The order of the district court (J.S. App. 1a-6a) is unreported.

JURISDICTION

The judgment of the district court (J.S. App. 7a) was entered on January 23, 1985. A notice of appeal to this Court (J.S. App. 8a) was filed on February 21, 1985. On April 16, 1985, Justice Stevens extended the time for docketing the appeal to and including June 21, 1985. The jurisdictional statement was filed on that date, and probable jurisdiction was noted on October 7, 1985 (J.A. 23). The jurisdiction of this Court is invoked under 28 U.S.C. 1252. A direct appeal lies where, as here, a federal statute

has been held unconstitutional as applied. *United States* v. *Darusmont*, 449 U.S. 292, 293 (1981) (per curiam).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

The relevant constitutional and statutory provisions are set forth in the appendix to the jurisdictional statement (J.S. App. 9a-11a).

STATEMENT

In 1976, Congress significantly changed the relationship between the federal gift tax and the federal estate tax. Previously, a taxpayer had been entitled to a lifetime "specific exemption" of $30,000 for gift-tax purposes, and his estate had been entitled to an exemption of $60,000 for estate-tax purposes. In 1976 Congress brought a measure of unification to the gift tax and the estate tax, and in the course of doing so it replaced those two separate exemptions with a single "unified credit," which was made available against either or both taxes, as first incurred. In an effort to produce an orderly transition from the earlier tax regime to the later, Congress provided that a person (or the estate of a person) who had claimed some or all of his lifetime "specific exemption" for certain gifts could not later claim the full "unified credit" against the gift or estate tax. Rather, the "unified credit" in such circumstances was required to be reduced to reflect the transfer tax benefit that the transferor had already garnered. The district court held that this transitional rule as applied in this case was a species of retroactive legislation, and that it was so arbitrary and capricious as to render it unconstitutional under the Due Process Clause of the Fifth Amendment.

A. The Statutory Framework

1. Prior to 1977, the estate tax and the gift tax, while functionally related, were separately imposed, separately administered, and separately collected. The gift tax was and is recurrent (*i.e.*, imposed and collected on an annual or quarterly basis) and, to guarantee progressivity, it has always been cumulative. The cumulation is accomplished by aggregating all taxable gifts made by a taxpayer after June 6, 1932, and through the taxable period in which subsequent gifts are made, in order to determine the tax rate or "bracket" applicable to a particular gift. See 26 U.S.C. 2502.[1] The gift tax provided an annual per-donee exclusion in a fixed dollar amount; in 1976, the exclusion was $3,000 per donee. 26 U.S.C. (1976 ed.) 2503(b).[2] The gift tax also provided a lifetime "specific exemption"—basically a deduction—in the amount of $30,000 (26 U.S.C. (1970 ed.) 2521). A taxpayer could claim the specific exemption, in whole or in part, whenever he chose.

The estate tax, of course, has never been recurrent, but is imposed at graduated rates on the "taxable estate" (26 U.S.C. 2051). The taxable estate has always been defined to include, not only property owned by the decedent at his death, but also certain property

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[1] The cumulation begins with June 6, 1932, the date the present gift tax was imposed. Revenue Act of 1932, ch. 209, Tit. IV, 47 Stat. 245 *et seq.* A noncumulative gift tax had previously been imposed by the Revenue Act of 1924, ch. 234, 43 Stat. 253 *et seq.*; it was repealed by the Revenue Act of 1926, ch. 27, § 1200(a), 44 Stat. 125.

[2] The $3,000-per-donee annual exclusion was established by the Revenue Act of 1942, ch. 617, § 454, 56 Stat. 953. It has since been increased to $10,000. Economic Recovery Tax Act of 1981, Pub. L. No. 97-34, § 441(a), 95 Stat. 319.

that he may have transferred during life, or which is subject to transfer under specified circumstances relating to his death. In 1976, the estate tax provided a $60,000 exemption—again, basically a deduction—in determining the taxable estate (26 U.S.C. (1970 ed.) 2052).

Although the gift tax and the estate tax were separate in most aspects, and although gift tax rates prior to 1977 were only 75% of estate tax rates on comparable transfers, the two taxes were never entirely unconnected. From the beginning, it was clear that some property, the lifetime transfer of which was subject to the gift tax, might also be includable in the transferor's estate for estate tax purposes. Common examples were gifts in contemplation of death (26 U.S.C. (1970 ed.) 2035) and transfers with a retained life interest (26 U.S.C. (1970 ed.) 2036). To alleviate the double tax burden in such situations, Congress provided that, where the transfer of property includable in the gross estate had previously been subject to gift tax, a credit was allowable against the estate tax for the gift tax paid (26 U.S.C. (1970 ed.) 2012).[3]

2. In the Tax Reform Act of 1976, Pub. L. No. 94-455, Tit. XX, 90 Stat. 1846 *et seq.*, Congress substantially integrated the estate tax and the gift tax without greatly altering the coverage of either. The first step was to bring the two rate structures into conformity. This was done by making gift tax rates

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[3] Because of possible differences in value at the time of the gift and at the time of decedent's death, differences in the amounts of the taxable estate and of the aggregate of taxable gifts, and differences in rates and structures, computation of the gift tax credit may be complex, to say the least. See Treas. Reg. § 20.2012-1 (1970).

equal to estate tax rates.[4] Then, in lieu of the $30,000 specific exemption from the gift tax and the $60,000 exemption from the estate tax, Congress created, not an exemption or deduction, but a credit against the taxes imposed, termed the "unified credit," available against either or both taxes as first incurred.[5] Finally, a somewhat intricate mechanism for a degree of unification was supplied by providing that the estate tax should be determined (subject to the "unified credit") by a computation that first aggregated the taxable estate and taxable gifts made after December 31, 1976; computed a tax on that aggregate sum; and then reduced the result by the gift tax payable on the gifts thus included.[6] Roughly speaking, the result was to treat the taxable estate as the "ultimate taxable gift." See generally J. McCord, *1976 Estate and Gift Tax Reform: Analysis, Explanation and Commentary* (1977).

The 1976 Act was effective with respect to estates of decedents dying after December 31, 1976, and with respect to gifts made after that date. But while the Act inaugurated a measure of integration, it did not purport to provide a completely fresh start, and could hardly have done so. Continuity with the past necessarily had to be provided for. The estate of a decedent dying after 1976, for example, would continue

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[4] Pub. L. No. 94-455, § 2001(b)(1), 90 Stat. 1849 (amending 26 U.S.C. 2502(a)).

[5] Pub. L. No. 94-455, § 2001(a)(2), (3) and (4), 90 Stat. 1848 (adding 26 U.S.C. 2010, amending 26 U.S.C. 2012 and repealing 26 U.S.C. (1970 ed.) 2052); Pub. L. No. 94-455, § 2001(b)(2) and (3), 90 Stat. 1849 (adding 26 U.S.C. 2505 and repealing 26 U.S.C. (1970 ed.) 2521).

[6] Pub. L. No. 94-455, § 2001(a)(1), 90 Stat. 1846 (amending 26 U.S.C. 2001).

in many cases to include assets that he had disposed of before 1977, such as property transferred in contemplation of death or with a retained life interest. Where such prior transfers had been subject to gift tax, the gift tax previously paid would produce a credit against the post-1976 estate tax. And because the gift tax itself remained recurrent and cumulative, gifts made before 1977 continued to affect the impact of the new and higher gift tax rates applicable to gifts made during or after that year. See 26 U.S.C. 2501(a), 2502.

Most relevant for present purposes, a nettlesome question of continuity arose from the fact that the $30,000 specific exemption from the gift tax, which a taxpayer could have employed at the time or times of his choice, was, together with the $60,000 exemption from the estate tax, to be repealed, and the new "unified credit," applicable against either or both taxes, substituted therefor. Obviously, some taxpayers would have employed all or part of the $30,000 specific exemption against pre-1977 gifts. The question was whether that fact should call for an adjustment in the unified credit that they or their estates might subsequently claim.

The bill reported by the House Ways and Means Committee on August 6, 1976, answered that question in the affirmative. It provided that if the specific exemption had been claimed in whole or in part by a taxpayer after June 6, 1932, the unified credit otherwise allowable was to be reduced by 20% of the amount so claimed. H.R. 14844, 94th Cong., 2d Sess. §§ 2010(c), 2505(c) (1976) (set forth at H.R. Rep. 94-1380, 94th Cong., 2d Sess. 94, 131 (1976)). The Committee explained its proposal as follows (H.R. Rep. 94-1380, *supra*, at 16):

> As a transitional rule, the unified credit allowable is to be reduced by an amount equal to 20 percent of the amount allowed as a specific exemption in computing taxable gifts under present law. Thus, in the case where a donor had benefited from the use of the full $30,000 gift tax specific exemption under present law, the maximum unified credit allowable would be reduced by $6,000.

Although the legislative history does not address the matter, the 20% figure was apparently chosen because it was thought to approximate the average effective gift tax rate, and thus to represent the average transfer tax benefit realized by persons who previously had claimed and been allowed some or all of the specific exemption.

The Conference Committee, in adding provisions of H.R. 14844 to the pending Tax Reform Act of 1976, limited the scope of this transitional rule. It agreed with the House that the new unified credit should be reduced on account of certain gifts as to which the specific exemption had been claimed. However, it decided that the reduction in the unified credit should operate, not in the case of all gifts made after June 6, 1932, but only in the case of gifts made after September 8, 1976—the date the Conference Committee approved the measure. The Committee reports do not explain the reason for thus limiting the scope of the transitional rule.[7] But the transitional rule, with the limitation added in conference, has uniformly

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[7] Each report states simply that "the unified credit is not to be reduced for any amount allowed as a specific exemption for gifts made prior to September 9, 1976." H.R. Conf. Rep. 94-1515, 94th Cong., 2d Sess. 607-608 (1976); S. Conf. Rep. 94-1236, 94th Cong., 2d Sess. 607-608 (1976).

been understood to serve the objective of removing the incentive to make large gifts during the period between September 8, 1976, and January 1, 1977—gifts that otherwise would have provided a double tax benefit in the form of a $30,000 specific exemption under the old regime coupled with an undiminished unified credit under the new. See *Estate of Gawne* v. *Commissioner*, 80 T.C. 478, 483 (1983); R. Stephens, G. Maxfield & S. Lind, *Federal Estate and Gift Taxation* ¶ 3.02, at 3-4 n.9 (5th ed. 1983); J. McCord, *supra*, § 2.13, at 26.

The Tax Reform Act of 1976, incorporating the limited transitional rule described above, was passed by both Houses of Congress on September 16, 1976. It was signed by the President on October 4, 1976. The transitional rule is currently codified in 26 U.S.C. 2010(c) and 2505(c).

B. The Proceedings In This Case

The facts were stipulated (J.A. 4-22), and the case was submitted to the district court on those stipulated facts (J.S. App. 2a). On September 28, 1976, Charles Hirschi made gifts aggregating $45,000 in value to five persons (*ibid.*). Two days later, he reported those gifts on a federal gift tax return, which indicated no tax due (*id.* at 2a-3a; J.A. 5, 8-13). The first $15,000 of his gifts, consisting of $3,000 transfers to each of the five recipients, was exempt from gift tax by virtue of the annual per-donee exclusion (26 U.S.C. (1970 ed.) 2503(b)). As to the $30,000 balance, Hirschi elected to apply the full amount of his lifetime "specific exemption," thus eliminating any tax (J.S. App. 2a; J.A. 5, 8-13).

Slightly more than two years later, on November 9, 1978, Hirschi died (J.S. App. 2a; J.A. 5). Appellee

Farmers & Merchants Bank filed a federal estate tax return on behalf of the estate (J.A. 5, 14). On Schedule G of that return, which is entitled "Transfers During Decedent's Life," appellee included in the gross estate, as transfers in contemplation of death, the $45,000 in gifts that Hirschi had made on September 28, 1976 (J.S. App. 2a; J.A. 6, 15-18). The estate claimed a unified credit of $34,000, the maximum amount allowable for estates of decedents dying in 1978. J.S. App. 2a; J.A. 14; see 26 U.S.C. (1976 ed.) 2010(b). On audit, the Internal Revenue Service determined that, since Hirschi had claimed a $30,000 specific exemption for gifts made after September 8, 1976, and before January 1, 1977, the unified credit allowable to his estate was required to be reduced by $6,000—20% of the $30,000 specific exemption previously claimed—under the transitional rule of Section 2010(c). The Commissioner accordingly proposed a deficiency in federal estate taxes in the amount of $6,000 (J.S. App. 2a; J.A. 6).

Appellees paid the $6,000 deficiency in July 1982. The following month, they filed a claim for refund of the tax thus paid (J.S. App. 2a; J.A. 7). Although the theory set forth in their refund claim was not entirely clear, they appeared to contend that, since the property that Hirschi had transferred in September 1976 had been included in the gross estate, Section 2010(c) should be interpreted so as not to require any reduction in the unified credit, even though Hirschi had elected to claim the $30,000 specific exemption with respect to those gifts (J.A. 20-22). Appellees argued that "it was not the intention of the drafters of the Internal Revenue Code" to require reduction of the unified credit in these circumstances, and asserted that the Commissioner's construction of

Section 2010(c) to require such a reduction produced "inequitable treatment" that "[i]n essence * * * results in double taxation" (J.A. 21).

Following the denial of their claim for refund, appellees brought this refund suit in the United States District Court for the Southern District of Illinois (J.S. App. 2a; J.A. 1). They again asserted that Section 2010(c) should be construed so as not to call for any reduction in the unified credit under the circumstances of this case. In a supplemental brief, appellees contended alternatively that, if Section 2010(c) were applied to require reduction of the unified credit on account of gifts made before the statute's enactment on October 4, 1976, it would to that extent be retroactive, and would on that ground violate the Fifth Amendment by depriving them of property without due process of law.[8]

The district court recited that "[t]he first issue raised by the plaintiffs which we will address concerns whether the retroactive provision of [26 U.S.C.] 2010 is unconstitutional and thus violates the due process clause of the Fifth Amendment" (J.S. App. 3a). The court acknowledged (*id.* at 3a-4a) that this Court has frequently upheld retroactive application of income tax legislation, but, on the asserted authority of *Shanahan* v. *United States*, 447 F.2d 1082 (10th Cir. 1971), concluded that those decisions do not apply to transfers subject to the estate and gift taxes.

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[8] Appellees' claim of unconstitutionality was based upon the undisputed facts, and the government did not contend that their argument represented an improper variance from the theory set forth in their administrative claim for refund. Cf. *Angelus Milling Co.* v. *Commissioner*, 325 U.S. 293 (1945); *Scovill Mfg. Co.* v. *Fitzpatrick*, 215 F.2d 567 (2d Cir. 1954). See Stip. para. 15 (J.A. 7).

Rather, the court said, this case was controlled by *Untermyer* v. *Anderson*, 276 U.S. 440 (1928), where the Court held that the federal gift tax, newly imposed in 1924, could not constitutionally be applied to gifts completed before its enactment. The district court acknowledged that, in *Milliken* v. *United States*, 283 U.S. 15 (1931), this Court subsequently upheld the constitutionality of an amended estate tax statute as applied to a previously-completed gift in contemplation of death, even though the amendment worked to the estate's disadvantage by imposing higher tax rates and requiring the previously-transferred property to be valued at a higher figure. But the district court found *Milliken* "distinguishable from the case at bar" and held that "the tax under Section 2010(c) as applied to this transaction is so arbitrary and capricious as to render it unconstitutional" (J.S. App. 5a, 6a). Accordingly, and without discussing their statutory construction argument, it entered judgment for appellees (*id.* at 7a).

SUMMARY OF ARGUMENT

The transitional rule incorporated in Section 2010(c) was designed to accomplish an orderly transition to the new estate-and-gift-tax regime that Congress enacted in 1976. The district court held that this transitional rule, as applied to appellees, was a species of retroactive legislation, and that its operation was so harsh as to deprive them of property without due process of law. The district court was wrong for at least four independent reasons.

First, the statute did not deprive appellees of property. As they concede (Mot. to Dis. 6), the overall effect of the Tax Reform Act of 1976, including Section 2010(c), was to "reduce[] the decedent's estate

tax by $655.16." This diminution of their tax liability can scarcely be called a deprivation of property.

Second, the statute was not "retroactive" legislation. The estate tax amendment that appellees challenge was enacted more than two years before the testator died. The amendment did require that, in computing the estate tax in 1978, his executors take into account the fact that he had claimed the specific exemption in 1976. But this Court has repeatedly rejected the idea that a tax is "retroactive" merely because its operation depends on facts or conditions that came into existence previously. Indeed, the operation of the estate tax regularly depends on actions that the decedent may have taken many years before his death. In characterizing Section 2010(c) as "retroactive" legislation, therefore, the district court evaluated its constitutionality under an erroneous premise.

Third, even if Section 2010(c) could properly be called a "retroactive" statute, its application to appellees was not "so harsh and oppressive as to be a denial of due process" (*United States* v. *Darusmont*, 449 U.S. 292, 299 (1981)). Its lack of harshness is particularly evident here, since the overall effect of the 1976 estate tax amendments was to save appellees money. More generally, the purpose of the transitional rule was to prevent taxpayers (or the estates of taxpayers) who had claimed the specific exemption under the old tax regime from deriving a double tax benefit from an unreduced "unified credit" under the regime that Congress enacted in 1976. The possibility of such a double tax benefit arose from the fact that the unified credit was a *substitute* for the specific exemption. It is well settled that due process is satisfied upon a "showing that the retroactive application

of the legislation is *itself* justified by a rational legislative purpose." *Pension Benefit Guaranty Corp.* v. *R.A. Gray & Co.*, No. 83-245 (June 18, 1984), slip op. 12 (emphasis added). The transitional rule involved here clearly represented a rational exercise of Congress's taxing power.

Finally, the decedent in this case "had ample advance notice" (*United States* v. *Darusmont*, 449 U.S. at 299) of the proposed change in the tax laws. The key congressional committees had issued reports explaining the transitional rule, and the bill in which it was incorporated had passed both houses of Congress, before the decedent made the gifts at issue. He thus had constructive if not actual notice of what the effect of claiming the specific exemption was likely to be.

ARGUMENT

THE TRANSITIONAL RULE INCORPORATED IN SECTION 2010(c) IS VALID AS APPLIED TO APPELLEES

A. There Is No Merit To Appellees' Statutory Argument, Or To Their Related Assertion That Section 2010(c) As Applied To Them Results In Double Taxation

Before addressing appellees' constitutional claim, it seems appropriate to dispel any confusion that may have arisen from certain statements that they made in their claim for refund, and again in their motion to dismiss. In their claim for refund, appellees asserted that Section 2010(c) as applied to them "results in double taxation" (J.A. 21). By this they appeared to mean that the effect of Section 2010(c) was to tax *twice* the property that the decedent transferred on September 28, 1976—first under the gift tax, and then, when the property was included in the

decedent's estate as a transfer in contemplation of death, again under the estate tax. Alternatively, appellees asserted that the inclusion of that property in the gross estate, when combined with the reduction in the allowable unified credit under Section 2010(c), "[in] effect results in a doubling of the 34% rate of [estate] tax" (J.A. 22). Appellees repeat both assertions, using slightly different words, in their motion to dismiss (Mot. to Dis. 6, 7).

There is no factual basis for these statements. The single tax that was assessed and paid with respect to the property transferred by the decedent in September 1976 was the estate tax paid after decedent's death in November 1978. No tax was paid with respect to the transfer of that property in 1976 because the decedent elected to apply the gift tax specific exemption of $30,000. That exemption, coupled with the applicable annual exclusions, meant that no gift tax was paid or payable with respect to the $45,000 transferred. When the property was subjected to estate tax by reason of the decedent's death in 1978, moreover, it was taxed, as the balance of his taxable estate in excess of $250,000 was taxed, at the marginal estate tax rate of 34%. See 26 U.S.C. (1976 ed.) 2001(c); J.A. 14. Appellees' assertions that the same property was taxed twice, or at double rates, are thus squarely contrary to fact.

In reality, appellees' assertions about "double taxation" and "double tax rates" are a factually erroneous way of characterizing—indeed, one might say, of dramatizing—the statutory construction argument that they presented first in their claim for refund and then to the district court. They argued that it would be "inequitable" to reduce the estate's unified credit on account of the decedent's 1976 gifts, even though

he had claimed and had been allowed the $30,000 specific exemption from gift tax with respect to those gifts, because he had the misfortune to die within the next three years, with the result that the property ended up being subject to tax anyway—albeit to estate tax rather than to gift tax—as a transfer in contemplation of death. See J.A. 21-22. In essence, appellees argued that they derived no benefit from the specific exemption, and hence that it would "penalize[] the unfortunate transferor" and his estate to invoke Section 2010(c) against them (J.A. 22). They accordingly urged that the statute be interpreted as inapplicable in these circumstances.

Appellees' statutory construction argument is meritless. The district court, while not addressing that argument specifically, rejected it sub silentio in reaching the merits of their constitutional claim. And their statutory argument has been explicitly rejected by the only other court that has considered it. *Estate of Renick* v. *United States*, 687 F.2d 371, 376-377 (Ct. Cl. 1982). On facts substantially identical to those here, the Court of Claims found meritless the contention "that § 2010(c) should be construed so that the reduction in the unified credit is restored when the gift is included in the gross estate [as a transfer in contemplation of death] pursuant to § 2035" (687 F.2d at 377). "The plain language and legislative design of § 2010(c)," the court noted, "show that Congress intended the reduction to the unified credit to occur in *all* cases where gifts were made during the transition period and the specific gift tax exemption * * * was taken by the donors" (687 F.2d at 376 (emphasis in original)). The court squarely rejected the notion that "Congress intended to reduce the unified credit only if the taxpayer had benefited" from

the exemption (*id.* at 377). "When the decedent made the gift," the court observed, "it *appeared* that he would benefit" from the exemption, and that appearance failed to become a reality only because of his untimely death (*ibid.* (emphasis added)). Although the decedent's untimely death might thus be said to have worked something of a tax advantage to his estate, the Court of Claims correctly refused to find that circumstance a sufficient justification to "imply an exception to the statute" that Congress did not provide (*id.* at 376).

Contrary to appellees' contention, moreover, the situation in which they find themselves is not "inequitable" at all. Prior to 1977, there had always been an element of gamble in a taxpayer's decision about whether and when to elect the $30,000 gift tax exemption. Since the gift tax was cumulative and progressive, with pre-1977 gift tax brackets ranging from 2¼% to 57¾% (26 U.S.C. (1976 ed.) 2502), it made economic sense for a taxpayer who contemplated making substantial gifts to defer claiming the exemption, since it would eliminate considerably more in gift taxes if applied against later gifts subject to tax in the higher brackets than if it were applied to earlier gifts subject to tax in the lower brackets. Deferring the election, on the other hand, created the alternative risks that the taxpayer would die before ever claiming it, or that he would fail to survive for three years after claiming it, in which case the gift as to which it was claimed would be included in his gross estate as a transfer in contemplation of death. In either of the latter events, the specific exemption would basically be wasted.

In this case, as matters eventuated, it would have been better for Hirschi and his estate had he not claimed the specific exemption for the gifts he made

on September 28, 1976, but had rather paid the $2,250 in gift tax that would then have been due. See 26 U.S.C. (1970 ed.) 2502. In that event, his estate would have had credited against the estate tax the $2,250 gift tax paid (26 U.S.C. 2012), and would have enjoyed an unreduced unified credit of $34,000. On the other hand, had Hirschi survived three years after making his gifts, the $45,000 in property that he gave away in 1976 would have been excluded from his taxable estate, and the estate tax due from his executors would have been reduced accordingly. See 26 U.S.C. (1976 ed.) 2001. As appellees acknowledge (Mot. to Dis. 8), Hirschi's gift tax return for the third quarter of 1976 was not due until November 15 of that year. But for his unusual haste, therefore, in filing his return two days after making his gifts, he could have waited a week to see if the President signed the 1976 Act, and then computed the relative advantages and disadvantages of claiming the exemption, in view of the uncertainties of life. If the situation in which appellees find themselves is "inequitable," in other words, the inequity stems, not from the Internal Revenue Code, but from the fact of human mortality.

B. The Application Of The 1976 Act To The Hirschi Estate Did Not Deprive Appellees Of Property

Although the decedent in this case died in November 1978, the district court characterized the application of the estate tax provisions of the 1976 Act, including Section 2010(c), as retroactive, and for that reason violative of the Due Process Clause of the Fifth Amendment (J.S. App. 3a-6a). But the application of that law, however characterized, deprived appellees

of no property, with or without due process. The estate tax return filed by appellees reported a taxable estate of $402,242.10 (J.A. 14). They claimed a unified credit of $34,000, and reported estate tax due of $81,690.56 (*ibid.*). The Commissioner accepted the return as filed, except that he reduced the unified credit from $34,000 to $28,000, as he was required to do by Section 2010(c). He accordingly assessed a deficiency of $6,000, resulting in an estate tax of $87,690.56. If the provisions of the estate tax as it stood in September 1976 had been applied to the same taxable estate, however, the estate tax would have been $88,345.72. See 26 U.S.C. (1970 ed.) 2001. As appellees concede, therefore, "[t]he Tax Reform Act [of 1976] reduced the decedent's estate tax by $655.16" (Mot. to Dis. 6). This diminution of tax liability can hardly be said to have been "so arbitrary and capricious as to render [the law] unconstitutional," in the words of the district court (J.S. App. 6a), or in any fashion to have deprived the estate of property.

C. The District Court Mischaracterized Section 2010(c) As Retroactive Legislation

Contrary to the district court's statement (J.S. App. 3a), Section 2010(c) as applied to appellees does not constitute "retroactive" legislation, and the court thus proceeded from an erroneous premise in holding it unconstitutional. When the decedent made his gifts in September 1976, he received the benefit of the then-existing $30,000 specific exemption for gift tax purposes. The Tax Reform Act of 1976 was signed by the President one week later, and thus became law more than two years before Mr. Hirschi

died. When he died, his estate received the benefit of the then-existing unified credit. It is true that the unified credit was reduced by virtue of his already having employed the gift tax specific exemption, which was one of the two items for which the unified credit was a substitute. But his estate derived considerably more value from the reduced credit of $28,000 than it would have derived from the $60,000 estate tax exemption that existed when he made his gifts.[9] In any event, this Court has regularly held that an estate tax provision that is effective at the date of death "does not operate retroactively merely because some of the facts or conditions upon which its application depends came into being prior to the enactment of the tax." *United States* v. *Jacobs*, 306 U.S. 363, 367 (1939) (footnote omitted). Accord, *United States* v. *Manufacturers National Bank*, 363 U.S. 194, 200 (1960).[10]

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[9] For an estate subject (as was the Hirschi estate) to a 34% marginal rate of tax, the $60,000 estate tax exemption in effect prior to 1977 would have reduced the estate tax otherwise due by $20,400. Under the Tax Reform Act of 1976, by contrast, the unified credit provided to the Hirschi estate reduced the estate tax due by $28,000.

[10] In *United States* v. *Jacobs*, the decedent had paid for property and had it conveyed to himself and his wife as joint tenants in 1909, seven years before the estate tax was first enacted in 1916 (306 U.S. at 364). He died after the Revenue Act of 1924 required that jointly held property be included in the gross estate of the decedent who had furnished the consideration for the transfer. The Court noted that the estate tax "was not levied on the 1909 transfer," but on the testamentary transfer that occurred after the estate tax was amended in 1924 (306 U.S. at 366). The Court accordingly held that the amendment "was not retroactive" (*ibid.*). In *United States*

Indeed, the application of the estate tax has regularly depended upon facts and conditions that may have come into being prior to the enactment of the tax. As noted above, the estate tax has never been limited to property owned by the decedent at the time of his death, but has always, in its original form and as amended, included in the decedent's gross estate some property transferred or otherwise acted upon by him at some earlier time. See, *e.g.*, 26 U.S.C. (1970 ed.) 2035 (transfers in contemplation of death); 26 U.S.C. 2036 (transfers with retained life estate); 26 U.S.C. 2037 (transfers taking effect at death); 26 U.S.C. 2038 (revocable transfers). This Court has never held that the estate tax operates "retroactively" simply because that earlier time was

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v. *Manufacturers National Bank*, the decedent in 1936 had divested himself of ownership of a life insurance policy at a time when that would have removed the policy or its proceeds from his gross estate (363 U.S. at 196). The decedent, however, continued to pay the premiums on the policy until he died (*ibid.*). He died in 1954, after the Revenue Act of 1942 made payment of premiums a test for inclusion of life insurance proceeds in a decedent's gross estate. The Court held that the 1942 amendment, having become effective long before the decedent died, "cannot be said to be retroactive in its impact"; the fact that "the policies were purchased and the policy rights were assigned before the [1942 amendment] was enacted," the Court stated, was "not material" (363 U.S. at 200). See also *Fernandez* v. *Wiener*, 326 U.S. 340, 354 (1945) (upholding estate tax amendment requiring that the entire pre-existing community estate in a community property state be included in the gross estate of the spouse first to die); *Gwinn* v. *Commissioner*, 287 U.S. 224 (1932). If none of the cases summarized above involved retroactivity—and the Court uniformly stated that they did not—it is clear that the district court erred in characterizing the application of Section 2010(c) as retroactive here.

a time before the enactment of the estate tax provision dictating how such property or its transfer should be treated for federal estate tax purposes. See, *e.g.*, *Commissioner* v. *Estate of Church*, 335 U.S. 632 (1949); *Fernandez* v. *Wiener*, 326 U.S. 340 (1945); *Helvering* v. *Hallock*, 309 U.S. 106 (1940); *United States* v. *Jacobs*, 306 U.S. 363 (1939); *Gwinn* v. *Commissioner*, 287 U.S. 224 (1932); *United States* v. *Wells*, 283 U.S. 102 (1931).

D. The District Court Erred In Equating Retroactivity With Unconstitutionality

Even if the 1976 Act, with its enactment of Section 2010(c), were thought to have deprived appellees of property, and to have operated "retroactively" by virtue of its look-back feature, its effect was not so harsh or oppressive as to render it unconstitutional under the Due Process Clause. This Court has squarely rejected the idea that retroactivity in an estate tax statute, any more than in an income tax statute, perforce invalidates it. The Court has held that "a tax is not necessarily and certainly arbitrary and therefore invalid because retroactively applied," and has noted that "taxing acts having retroactive features have been upheld in view of the particular circumstances disclosed and considered by the Court." *Milliken* v. *United States*, 283 U.S. 15, 21 (1931). The Court in *Milliken* upheld the application of higher tax rates, imposed by an amended estate tax statute, to a previously-completed gift in contemplation of death, and also held that the gift could be valued for estate tax purposes at the date of death rather than at the time the gift was made.

This case involves a transitional rule designed to prevent taxpayers from manipulating the timing of

their gifts so as to derive a double tax benefit from the shift to a unified credit estate-and-gift tax regime. The decedent, having elected on September 30, 1976, to claim the full $30,000 specific exemption then permitted to him, had no claim to any further exemption on that score. Under the version of the transitional rule adopted by the House Ways and Means Committee, neither he nor his estate would have been entitled to any further exemption, or to its equivalent in the form of an undiminished unified credit, with respect to gifts that he had made at any time after June 6, 1932. See pages 6-7, *supra*. He and his estate gained no greater entitlement by virtue of the Conference Committee's decision to limit the application of the transitional rule to gifts made after September 8, 1976. That decision might be thought to have conferred a windfall upon certain taxpayers who had the good fortune to make gifts before the Conference Committee acted. But the Committee's decision not to extend that windfall to taxpayers who made gifts between September 8, 1976, and January 1, 1977, was plainly not "so harsh and oppressive as to be a denial of due process." *United States* v. *Darusmont*, 449 U.S. 292, 299 (1981). Such line-drawing is an inherent feature of tax legislation. See *United States* v. *Maryland Savings-Share Insurance Corp.*, 400 U.S. 4 (1970).[11]

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[11] Accord, *e.g.*, *Estate of Renick* v. *United States*, 687 F.2d at 374-376 (rejecting due process challenge to Section 2010(c)). Cf. *Reed* v. *United States*, 743 F.2d 481, 485-486 (7th Cir. 1984), cert. denied, No. 84-866 (June 3, 1985) (rejecting due process challenge to retroactive application of 1978 estate tax amendment); *Fein* v. *United States*, 730 F.2d 1211, 1212-1214 (8th Cir. 1984), cert. denied, No. 84-182 (Oct. 1, 1984) (same); *Estate of Ceppi* v. *Commissioner*,

In holding Section 2010(c)'s transitional rule unconstitutional as applied to appellees, the district court (J.S. App. 4a) relied chiefly on *Untermyer* v. *Anderson*, 276 U.S. 440 (1928). As this Court has repeatedly pointed out on the frequent occasions when it has distinguished that decision, however, *Untermyer* involved the retroactive application of the first gift tax statute—a wholly new tax enacted in 1924—to gifts irrevocably completed before its effective date. See, *e.g.*, *United States* v. *Darusmont*, 449 U.S. at 299-300 (distinguishing *Untermyer*); *Milliken* v. *United States*, 283 U.S. at 21 (same). Following this Court's lead, the courts of appeals, if not questioning the continuing vitality of *Untermyer*, have uniformly viewed it as applying only to the retroactive application of a wholly new tax.[12] The *Untermyer* decision

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698 F.2d 17, 20-22 (1st Cir.), cert. denied, 462 U.S. 1120 (1983) (same).

[12] See, *e.g.*, *Fein* v. *United States*, 730 F.2d at 1213-1214 ("the modern trend of decisions has uniformly been to limit" *Untermyer* to the "narrow situation" there involved); *Estate of Ceppi* v. *Commissioner*, 698 F.2d at 21 (collecting cases and concluding that, in light of this Court's subsequent decision in *Milliken*, "*Untermyer* at best remains good law only for the proposition that a wholly new gift tax cannot be applied retroactively"); *Westwick* v. *Commissioner*, 636 F.2d 291, 292 (10th Cir. 1980) (limiting *Untermyer* to "wholly new types of taxes"); *Buttke* v. *Commissioner*, 625 F.2d 202, 203 (8th Cir. 1980) (reading *Untermyer* to bar "retroactive application of a wholly new tax"), cert. denied, 450 U.S. 982 (1981); *Sidney* v. *Commissioner*, 273 F.2d 928, 932 (2d Cir. 1960) (Friendly, J.) ("If Untermyer remains authority at all, it is so only for the particular situation of a wholly new type of tax."). See generally Hochman, *The Supreme Court and the Constitutionality of Retroactive Legislation*, 73 Harv. L. Rev. 692 (1960); Ballard, *Retroactive Federal Taxation*, 48 Harv. L. Rev. 592 (1935).

has no bearing upon this case, which involves, not only an amendment to an existing tax, but an amendment that was enacted two years before the taxable event—the transfer of property upon the decedent's death—occurred.

E. Congress Provided Ample Advance Notice Of The Transitional Rule That It Enacted, And This Fact Eliminates Any Basis For A Claim Of Objectionable Retroactivity

Even if one were to accept appellees' contention that Section 2010(c) operates retroactively as applied to them, the decedent in this case "had ample advance notice" (*United States* v. *Darusmont*, 449 U.S. at 299) of the proposed change in the tax laws. The House Ways and Means Committee approved its version of the transitional rule on August 6, 1976. The Conference Committee approved on September 8, 1976, the version that was eventually enacted. The bill passed both houses of Congress on September 16, 1976. All these events occurred before the decedent made his gifts on September 28, 1976. The pattern of those gifts—exactly $45,000 to five family members (J.A. 15-18), tailored precisely to consume the specific exemption and the available annual exclusion —raises the irresistible inference that the decedent planned the transaction with tax considerations in mind, if it does not suggest that he had actual notice of the pending congressional action. In any event, the Committee reports provided him with constructive notice of what the effect of claiming the specific exemption was very likely to be. This Court has regularly held that there is no constitutional impediment to making a statute effective, as here, from the date of public notice. *Pension Benefit Guaranty Corp.* v. *R.A. Gray & Co.*, No. 83-245 (June 18, 1984), slip

op. 13-14 ("assuming that advance notice of legislative action with retrospective effects is constitutionally compelled, * * * we believe that employers had ample notice" of the contingent liability imposed by an amended pension statute); *United States* v. *Darusmont*, 449 U.S. at 299 (same, amended tax statute); *United States* v. *Hudson*, 299 U.S. 498 (1937).

Especially should this be so where, as here, a provision with retrospective aspects is adopted to prevent a "rush to the door" by persons seeking to circumvent the accomplishment of the purpose of the legislation. See *Pension Benefit Guaranty Corp.* v. *R.A. Gray & Co.*, slip op. 10-13.[13] It is well settled that "[t]he retroactive aspects of legislation * * * meet the test of due process * * * simply [upon a] showing that the retroactive application of the legislation is *itself* justified by a rational legislative purpose" (*id.* at 12 (emphasis added)). It was entirely rational for Congress to remove the incentive for taxpayers to seek the double tax benefit of a $30,000 gift tax exemption, plus an undiminished unified credit, by making gifts after September 8, 1976, and before the January 1, 1977, effective date of the new law.

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[13] See also *Purvis* v. *United States*, 501 F.2d 311 (9th Cir. 1974), cert. denied, 420 U.S. 947 (1975) (sustaining application of the interest-equalization tax, designed to stem outflow of investment capital from the United States, retroactively to transactions consummated during the year after introduction of the legislation); *First National Bank* v. *United States*, 420 F.2d 425 (Ct. Cl.), cert. denied, 398 U.S. 950 (1970) (same).

CONCLUSION

The judgment of the district court should be reversed.

Respectfully submitted.

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